No. 08-310

In The Supreme Court of the United States

POLAR TANKERS, INC.,
Petitioner,

v.

CITY OF VALDEZ,
Respondent.

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF ALASKA

BRIEF OF AMICUS CURIAE OF NATIONAL FEDERATION OF INDEPENDENT BUSINESS SMALL BUSINESS LEGAL CENTER IN SUPPORT OF PETITIONER

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INTEREST OF AMICUS CURIAE

Amicus, National Federation of Independent Business (NFIB) Small Business Legal Center,[1] is the legal voice of small business in America. As the legal arm of NFIB, the Small Business Legal Center represents the interests of small business in the nation's courts. The Small Business Legal Center participates in precedent setting cases that will have a critical impact on small businesses nationwide, such as the case before the Court in this action.

NFIB is an organization of more than 350,000 members, located in all 50 states. The members of NFIB are the small businesses that make up the backbone of the American economy. Small businesses account for more than 99 percent of all employers in the country and provide more than one-half of all jobs in our economy. More importantly, two-thirds of new job growth comes from small business. According to the United States Small Business Administration, small business accounts for more than half of the private non-farm gross domestic product in America. United States Small Business Administration, FAQs: Frequently Asked Questions, http://web.sba.gov/faqs/faqindex.cfm?areaID=24 (last visited Jan. 13, 2009).

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[1] Pursuant to this Court's Rule 37.3(a), all parties have consented to the filing of this brief. Letters evidencing such consent have been filed with the Clerk of the Court. Pursuant to Rule 37.6, Amicus Curiae affirms that no counsel for any party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than Amicus Curiae, its members, or its counsel made a monetary contribution to its preparation or submission.

In addition to providing goods and services in every sector of the economy (including exporting goods to other countries), NFIB members bear a significant portion of the overall national tax burden. In pursuit of its goal to support small business in America, NFIB and the NFIB Small Business Legal Center, which was formerly known as the NFIB Legal Foundation, have participated as amicus curiae in several cases before this Court including *Ledbetter v. Goodyear Tire & Rubber Co., Inc.*, 127 S. Ct. 2162 (2007), *Rapanos v. United States*, 547 U.S. 715 (2006), *Ballard v. Comm'r of Internal Revenue*, 544 U.S. 40 (2005), *Walters v. Metro. Educ. Enters., Inc.*, 519 U.S. 202 (1997), *Pierce v. Underwood*, 487 U.S. 552 (1988), and *Marshall v. Barlow's, Inc.*, 436 U.S. 307 (1978).

This case is of particular interest to small businesses, on which the greatest burden of new complex taxing schemes often falls. Small business owners most often identify tax-related regulations as the most burdensome type of regulations with which they must comply. William J. Dennis, Jr., *Coping with Regulation*, National Small Business Poll, Vol. 1, Issue 5, 2001, *available at* http://www.411sbfacts.com/sbpoll.php?POLLID=0038&KT_back=1.

Because a complex and unfair tax system and burdensome taxes are among the top concerns of small business owners, NFIB is committed to securing fair and equitable tax laws for its members, and ensuring that legislatures abide by constitutional requirements in passing such tax laws. Because the tax at issue in this case is levied

unfairly and in violation of constitutional principles, NFIB has an interest in this case.

SUMMARY OF ARGUMENT

Whether or not the tax at issue violates the Tonnage Clause, the apportionment formula used violates both the Fourteenth Amendment's Due Process Clause and the Commerce Clause of the Constitution. U.S. Const. art. I, § 8, cl. 3. These clauses forbid taxes on extraterritorial values and taxes that impose the risk of multiple taxation. The apportionment formula used by the City of Valdez does both. It creates the risk of multiple taxation and reaches extraterritorial values.

A business's state of domicile may tax all property values that have not attained a tax situs elsewhere. Insofar as Valdez's tax reaches value for time spent beyond its borders, the risk of multiple taxation exists. Small businesses are particularly vulnerable to the risk of multiple taxation since the burden rests with the taxpayer to show that property may be taxed elsewhere. The inordinate expense and time needed to contest a complex tax, such as the Valdez apportionment formula, makes it unlikely that a small entity would undertake such a challenge.

These extraterritorial taxes are not fairly apportioned to the benefits afforded by the taxing state, as required by the Due Process and Commerce Clauses. The benefits the City of Valdez claims it affords the shipping companies are entirely unavailable while the vessels are on the high seas.

A tax, therefore, that reaches value for time spent on the high seas is not fairly apportioned and thus is in violation of the Constitution.

ARGUMENT

I. THE VALDEZ APPORTIONMENT FORMULA CREATES A RISK OF MULTIPLE TAXATION THAT RENDERS THE TAX INVALID UNDER THE COMMERCE AND DUE PROCESS CLAUSES

A. The Domicile State Retains the Right to Tax the Vessels for the Time Spent on the High Seas, and Non-Domiciliary Jurisdictions Must Not Tax This Same Value

The state of domicile only loses its taxing power to the extent that the property has attained a tax situs elsewhere. *See Central R.R. Co. of Pa. v. Pennsylvania*, 370 U.S. 607, 611-612 (1962). The domicile state may then tax the value of property for all time it is not in another tax situs, including time spent on the high seas. Indeed, from the burden of proof provided in *Central Railroad*, there is a presumption that the domicile state may tax the entire value of the property. Specific property is only exempted when the taxpayer shows that "some portion of its total assets" may be taxed elsewhere. *Id.* at 613.

If another jurisdiction may also tax the property, the risk of multiple taxation arises. *Id.* at

612. Because the Due Process and Commerce Clauses forbid multiple taxation, the non-domiciliary jurisdiction must only tax the portion of the value of the property that has attained a tax situs there. Unconstitutional multiple taxation occurs if the non-domiciliary jurisdiction attempts to tax values that reflect more than the time the property actually spent within the jurisdiction. Here, the apportionment formula effectively taxes not only the value of the vessels for the time they spend in the City of Valdez's jurisdiction, but also the value of the vessels for some portion of the time spent on the high seas. The apportionment formula renders the tax invalid, as it creates the risk of multiple taxation.

The Alaska Supreme Court erred when it relied on *Japan Line v. County of Los Angeles*, 441 U.S. 434 (1979), to reach its decision. The Alaska Supreme Court determined that *Japan Line* precluded taxation by the domicile state for the period when property has no tax situs. *City of Valdez v. Polar Tankers, Inc.*, 182 P.3d 614, 620 n.26 (Alaska 2008). Therefore, under the Alaska court's reasoning, the domicile state is treated no differently from other taxing jurisdictions under *Japan Line*, and all jurisdictions gaining tax situs may tax equally the time spent on the high seas. *City of Valdez*, 182 P.3d at 620 ("Our determination that Valdez has adopted one of the many potential fair apportionment schemes it could choose from renders Polar's assertion of home port superiority irrelevant.").

This is neither a correct statement of the rule in *Japan Line* nor a logical consequence of it. *Japan Line* concerned the constitutionality of an *ad valorem* property tax on foreign-owned property in international commerce. *Japan Line*, 441 U.S. at 435. In declaring that "the home port doctrine . . . has yielded to a rule of fair apportionment among the states," this Court merely stated that movable property can be taxed by its domiciliary state and also by other states through which that property travels. *Id.* at 442. Oceangoing vessels had previously been exempted from apportionment schemes and remained subject to tax only by the domiciliary state. *Id.*

As the case was decided on other grounds, *Japan Line* did not determine whether the apportionment formulas replaced the home port doctrine for domestic oceangoing vessels. *Japan Line*, 441 U.S. at 443. In fact, the decision noted that this Court traditionally permitted the domicile state of oceangoing vessels to tax the entire value of the ship, rather than risk apportioning time spent on the high seas to non-domiciliary jurisdictions through which the vessel may travel. *Id.* at 442. Thus, this Court has long respected the rights of the domicile state to tax the time a vessel spends on the high seas. The dicta of *Japan Line,* on which the Alaska Supreme Court relied, at most suggests that fair apportionment should be applied to oceangoing vessels, an issue which is not debated in the present case. Fair apportionment does not require that the domicile state lose its right to tax the values of property having no other tax situs.

B. Small Businesses Face a Greater Risk of Multiple Taxation Than Large Businesses When Subjected to Invalid Apportionment Formulas

Subtle apportionment formulas that allow extraterritorial taxing create a greater risk of multiple taxation for small businesses. The burden rests with the taxpayer to show that its property may be taxed in another jurisdiction and is thus outside the taxing power of the domicile state. *Central R.R. Co. of Pa. v. Pennsylvania*, 370 U.S. 607, 613 (1962). For large businesses with sophisticated resources and teams of lawyers and accountants, determining and proving that some portion of the value of their property may be subject to tax elsewhere and then challenging the tax may well be a feasible task. The difficulty of identifying a risk of multiple taxation is compounded for small businesses with few resources and limited interstate commerce expertise. Of those small businesses that can identify the risk, even fewer will have the extensive resources necessary to bring their cases to court or carry their burdens of proof in complex tax litigation.

Tax complexity is a great burden to America's small businesses, and one that is increasing rapidly. Courts help small businesses when unnecessary complexity is eliminated and tax schemes are made as intuitive as possible. Here, the complexity of the tax also increases the risk of unconstitutional multiple taxation. A small business could predict that its property is subject to tax by other states for

the time it is physically present in those states. It is not predictable, nor indeed should it be, that the property would be subject to tax by other states for times it is outside the borders of those states. Because small businesses often do not have the means to readily identify or to challenge an apportionment formula that taxes for time spent outside of the jurisdiction, these businesses are at a much greater risk of multiple taxation.

II. THE VALDEZ APPORTIONMENT FORMULA TAXES EXTRATERRITORIAL VALUES IN VIOLATION OF THE COMMERCE AND DUE PROCESS CLAUSES

A non-domiciliary jurisdiction may only tax that portion of property that has attained a tax situs there and may not tax extraterritorial values. *See MeadWestvaco Corp. v. Illinois Dep't of Revenue*, 128 S. Ct. 1498, 1502 (2008). According to *Central Railroad*, a tax situs is established by "sufficient contact" with the jurisdiction. *Central R.R. Co. of Pa. v. Pennsylvania*, 370 U.S. 607, 615 (1962). It is not the entirety of the property, but rather "some determinable portion of the value" of the movable property that attains a tax situs in a non-domiciliary jurisdiction. *Id.* at 613. While the property is on the high seas, it has no contact with other jurisdictions, and thus it cannot acquire an extra-domiciliary tax situs. This means that while on the high seas, the vessels do not acquire a tax situs in the City of Valdez. To the extent that the apportionment formula captures time spent on the high seas, Valdez taxes extraterritorially.

The Due Process and Commerce Clauses require that the tax be "fairly apportioned" to the benefits provided by the taxing state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *Ott v. Mississippi Valley Barge Line Co.*, 336 U.S. 169, 174 (1949). The tax must "in practical operation [have a] relation to opportunities, benefits, or protection conferred or afforded by the taxing State." *Ott*, 336 U.S. at 174. While the vessels are in Valdez's port, the employees of the ships utilize municipal resources, including health care facilities and the airport. Brief in Opposition at 1, *Polar Tankers, Inc. v. City of Valdez*, No. 08-310 (Nov. 10, 2008). Hospitals, roads, and the airport are not used, however, when the ship is on the high seas. Thus a tax imposed for this time is not fairly apportioned.

Formulas from other cases that this Court has recognized to be fairly apportioned accurately reflect the time the property was present in the non-domiciliary jurisdiction. In *Ott v. Mississippi Valley Barge Line Co*, 336 U.S. 169, 171 (1949), the taxing authority calculated the challenged tax using a ratio of the number of miles of lines in Louisiana out of the total number of miles in the entire line. In *Standard Oil*, this Court recognized the *Ott* formula as "one which fairly apportioned the tax to the commerce carried on within the state." *Standard Oil v. Peck*, 342 U.S. 382, 383 (1952). In *Japan Line*, this Court ultimately struck down the tax. The decision approved, however, the apportionment formula applied by the non-domiciliary state of California, which roughly equaled the weeks the property was present in California. In approving

this calculation, this Court explained that "California effectively apportions its tax to reflect the container's 'average presence,' i.e., the time each container spends in the State per year." *Japan Line Ltd. v. County of Los Angeles*, 441 U.S. 434, 445 & n.8 (1979).

The Alaska Supreme Court found support for upholding the apportionment formula from *Braniff Airways* insofar as it viewed the apportionment formula used by Nebraska in *Braniff* and the formula used by the City of Valdez as analogous. *City of Valdez v. Polar Tankers*, 182 P.3d 614, 620-621 (Alaska 2008). In *Braniff Airways* an out-of-state air carrier subject to tax in Nebraska did not challenge the apportionment formula that Nebraska used, so the issue of the tax's reasonableness was not before the Court. *Braniff Airways v. Nebraska State Bd. of Equalization & Assessment*, 347 U.S. 590, 591 (1954). Moreover, the formula used in *Braniff* was the average of three ratios, only the first of which bears even a superficial similarity to the formula at issue in this case: (1) the ratio of landings and departures in Nebraska to all landings and departures per year; (2) the ratio of revenue tons handled at Nebraska airports to that handled by all airports per year; and (3) the ratio of originating revenue in Nebraska to all originating revenue per year. *Id.* at 593 n.4. The Alaska Supreme Court found that "[t]here is not too much difference between landings and dockings, nor between dockings and days in port." *City of Valdez*, 182 P.3d at 620. The court failed to appreciate, however, that every one of the air carrier's planes will make a stop at an airport virtually every day it is in operation.

Therefore, the ratio of landings in Nebraska to all landings would be essentially equal to days in Nebraska out of all days of operation. The distinction between daily airport landings and ships making port calls after weeks on the high seas negates any support from *Braniff*.

Small businesses are uniquely interested in seeing that the Commerce and Due Process Clauses are enforced in this area. Small businesses may be reluctant to engage in interstate commerce if non-domiciliary states can impose extraterritorial taxes. The uncertainty alone of what other states could tax may deter small businesses with limited resources from entering interstate commerce.

III. ALLOWING THIS TAX TO STAND WOULD HAVE DELETERIOUS POLICY CONSEQUENCES FOR SMALL BUSINESSES

A ruling that this tax is constitutional could negatively impact businesses across the country by encouraging other state and local governments to utilize similar apportionment formulas. Comparable taxes might, for example, affect smaller trucking or shipping firms that move across state lines.

When considering the constitutionality of this tax, this Court should be mindful of the complexity of the overall tax environment in which small businesses operate. In a 2008 survey of the problems and priorities facing small businesses, four of the top 10 ranked problems were tax related. Bruce D. Phillips & Holly Wade, NFIB Research

Foundation, *Small Business Problems and Priorities* 8 (2008). Property taxes – the category into which the challenged Alaska tax and other similar measures would fall – ranked fourth on the list. Twenty-five percent of small business owners polled indicated that property taxes are a critical problem. *Id.*

Tax complexity ranked fifth among small business owners' top concerns, with 23 percent of small business owners citing tax complexity as a critical problem for their businesses. *Id.* Navigating the federal and state tax codes has become so complex that 88 percent of small business owners now hire paid tax preparers or accountants. *Id.* Unsurprisingly, in another NFIB survey, small business owners identified tax-related regulations – federal, state, and local – as the most burdensome type of regulation. William J. Dennis, Jr., *Coping with Regulation*, National Small Business Poll, Vol. 1, Issue 5, 2001 at 1, *available at* http://www.411sbfacts.com/sbpoll.php?POLLID=0038&KT_back=1. *See also*, William J. Dennis, Jr., *Tax Complexity and the IRS*, National Small Business Poll, Vol. 6, Issue 6, 2006, *available at* http://www.411sbfacts.com/sbpoll.php?POLLID=0055 (analyzing small business owners' struggles with the Internal Revenue Code).

The costs of compliance with complex tax laws are immense, and small businesses bear a disproportionate share of the burden. In 2003, NFIB members reported spending an average of $74.24 per hour on tax related paperwork. William J. Dennis, Jr., *Paperwork and Record Keeping*, National Small Business Poll, Vol. 3, Issue 5, 2003, *available at* http://www.411sbfacts.com/sbpoll.php?POLLID=0010&KT_back=1. A Small Business Administration study also indicated that complex tax systems disproportionately burden small firms: the cost of tax compliance is 67 percent higher in small firms than it is in large firms. W. Mark Crain, United States Small Business Administration, Office of Advocacy, The Impact of Regulatory Costs on Small Firms (2005). In the only study available in the United States on the impact of tax-related paperwork on all firms by firm size, the Tax Foundation reported that the smallest firms spent 0.5 percent of their sales on tax compliance activity; the largest firms spent less than 0.1 percent of their sales on tax paperwork. *Cited in* United States Small Business Administration, Office of the Chief Counsel for Advocacy, The Changing Burden of Regulation, Paperwork, and Tax Compliance in the United States: A Report To Congress (1995). Similarly, a 1995 Hopkins and Diversified study showed that the smallest firms (those with fewer than 50 employees) spent closer to 5 percent of revenue on tax compliance costs. Cited in *Id.*

A decision to uphold the Valdez apportionment method would improperly expand local taxing authority at the expense of out-of-state interests and interstate commerce. Similar tax

apportionment methods would be eagerly adopted by other state and local governments looking to maximize tax revenue in today's tight economic climate. Such a result would negatively impact businesses of all sizes. Small business owners, however, would disproportionately feel the impact of such taxes as small firms are least able to navigate and challenge complex tax structures. Given that small business owners already operate within an exceedingly complex tax environment, any such additional taxes would feel like the proverbial extra straws pressing against the camel's back.

CONCLUSION

For the foregoing reasons, the judgment by the Alaska Supreme Court should be reversed.

Respectfully Submitted,

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